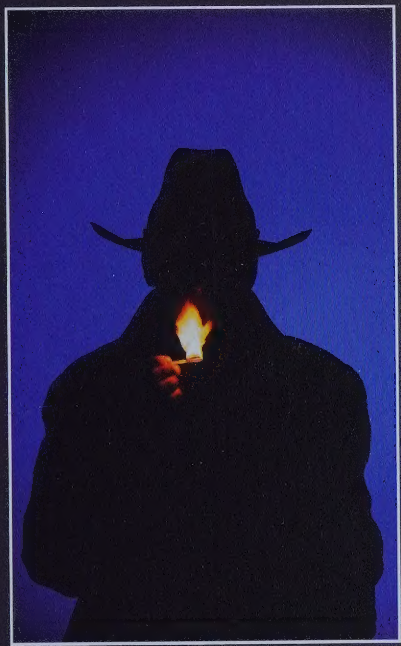


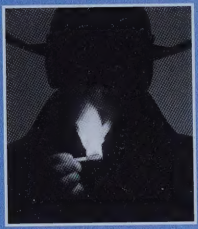
[Cigar Oil & Gas Ltd.]

[2001 Annual Report]

Contents

ANNUAL MEETING

Shareholders are cordially invited to attend the Company's Annual General Meeting which will be held at 3:00 PM on Tuesday October 30, 2001 in the Viking Room of the Calgary Petroleum Club, 319 - 5th Avenue S.W., Calgary, Alberta. Shareholders are requested to complete and return the Proxy Form to Computershare Trust Company of Canada at their earliest convenience if unable to attend the meeting.



Profile

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Corporate Profile

Cigar Oil & Gas Ltd. is a publicly traded junior oil & gas exploration, development and production company based in Calgary, Alberta.

Founded in 1987, the Company reorganized in 1999 with new directors and management and has continued to expand its production and reserve base in Western Canada.

Our corporate objective is to provide shareholders with continued per share growth in cash flow, earnings, production , reserves and net asset value. Cigar is listed on the Canadian Venture Exchange under the symbol "CGR".

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Fast Facts

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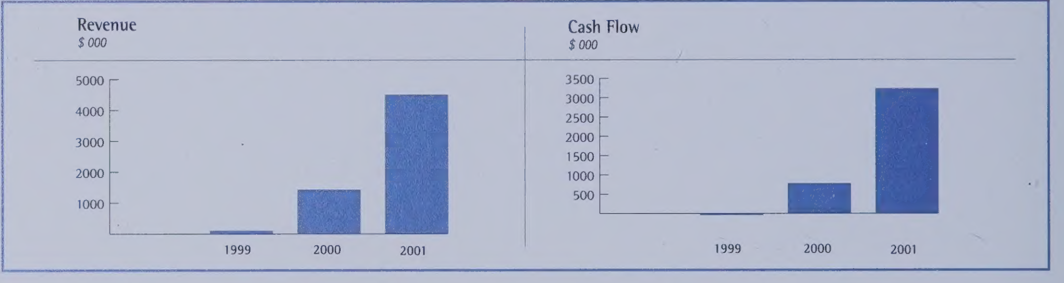
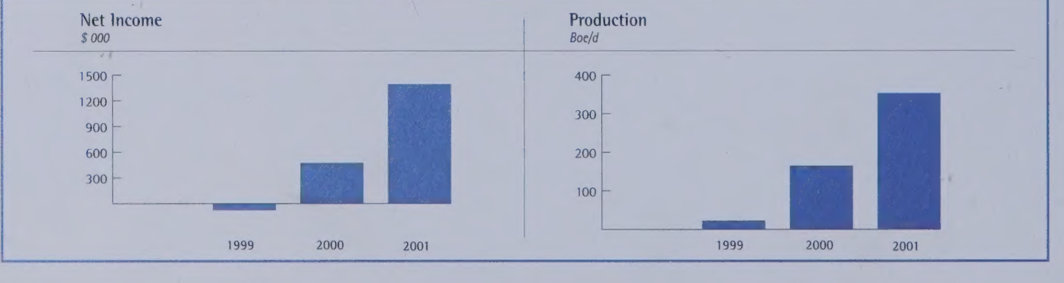
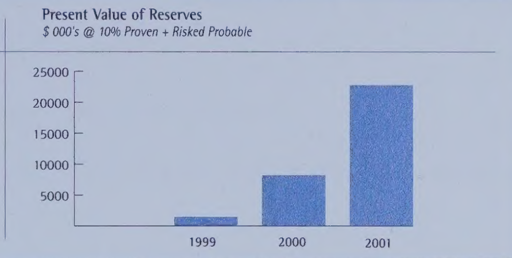
Report to our Shareholders

Fast Facts



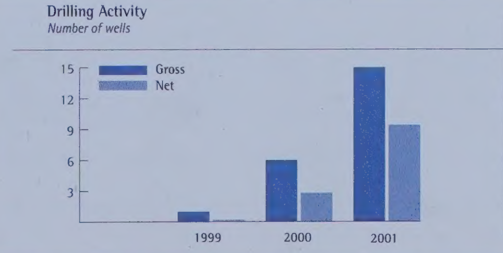
	2001	2000	Change
Financial results:			
Production revenue	$ 4,499,727	$ 1,428,465	215%
Cash flow from operations	$ 3,235,727	$ 781,078	314%
Per share - basic and diluted	$ 0.20	$ 0.05	300%
Net income	$ 1,390,962	$ 474,945	193%
Per share - basic and diluted	$ 0.09	$ 0.03	200%
Capital expenditures, net	$ 6,448,724	$ 3,367,364	92%
Debt and working capital (deficiency)	$ (1,817,704)	$ 235,628	
Ratio to annual cash flow	0.56:1	n/a	
Common shares outstanding at end of year			
Basic	17,611,639	15,771,639	12%
Diluted	19,661,639	16,871,639	17%

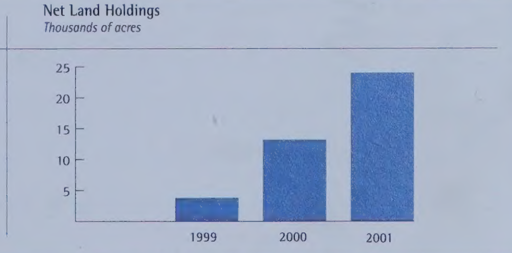




units as noted		2001	2000	Change
Operating results:				
Production	Crude oil (Bbls/d)	101	90	12%
	Natural gas (Mcf/d)	1,512	452	235%
	Oil equivalent (boe/d) (6:1)	353	165	114%
Average selling price	Crude oil and NGL's ($/Bbl)	$ 42.52	$ 36.18	18%
	Natural gas ($/Mcf)	$ 7.41	$ 3.68	101%
	Oil equivalent ($/Boe) (6:1)	$ 43.88	$ 29.74	48%
Cash flow netback ($/Boe)		$ 28.97	$ 17.66	64%
Operating expenses ($/Boe)		$ 5.58	$ 5.62	(1%)
General and administrative expenses ($/Boe)		$ 3.96	$ 5.91	(33%)
Proven and risked probable reserves				
Oil and liquids (Mbbls)		280	249	12%
Natural gas (Mmcf)		8,867	3,413	160%
Oil equivalent (Mboe) (6:1)		1,758	818	115%
Finding and on-stream costs ($/Boe)				
Proven		7.24	6.83	6%
Proven and risked probable		6.03	5.37	12%
Recycle ratio				
Proven		4.0	2.6	54%
Proven and risked probable		4.8	3.3	45%
Reserve replacement ratio				
Proven		6.9	8.2	(16%)
Proven and risked probable		8.3	10.4	(20%)
Undeveloped land	Gross acres	53,234	29,235	82%
	Net acres	24,003	13,156	82%
	Average working interest	45%	45%	

* *to comply with current industry practice, the Company is reporting natural gas production using a 6:1 equivalent instead of a 10:1 equivalent used in prior reporting periods, for comparative purposes fiscal 2000 has been restated using a 6:1 Boe conversion.*





Report to our shareholders

Fiscal 2001 proved to be an excellent year for Cigar Oil & Gas Ltd. The strategies for growth, initially established during 1999 and first implemented in 2000, continued to be pursued resulting in strong gains for our Company in all areas of our business. Maintaining our disciplined approach to the business we were again able to significantly increase the Company's reserves, production base and net asset value.

The Company has now positioned itself within several core areas in which we have built a stable production base and an inventory of new projects. These projects provide the Company with significant growth opportunities as we continue to execute our business plan.

2001 HIGHLIGHTS

> Our management team was strengthened with the addition of a VP Exploration and a Controller;

> Oil and gas revenues were up 215%;

> Cash flow from operations rose 314%;

> Net income increased 193%;

> Reserves increased from 818 Mboe to 1,758 Mboe, a 115% increase;

> The value of proven plus risked probable reserves, discounted at 10% increased 177%, from $8,223,000 to $22,778,000;

> Our natural gas bias was underscored with this product accounting for 71% (78% exit) of our average production;

> Capital expenditures of $6,448,700 added 1,069M Boe of reserves, at a cost of $6.03 per Boe – proven and risked probable;

> The Company's reserve replacement ratio was 8.3 times while the recycle ratio was 4.8:1 – proven and risked probable;

> Average return on equity was 31.3%;

> Dilution to shareholders resulting from new equity/stock options issued during the year was 12% notwithstanding, we attained a 300% increase in cash flow per share and 114% increase in production;

> Cigar's line of credit was doubled from $3.0 million to $6.0 million; and

> Our undeveloped land position increased by 82% from 13,156 net acres to 24,000 net acres, Cigar's interest averaged 45%.

ACTIVITIES

Acquisitions

Cigar spent $593,000 on two small but synergistic acquisitions during the year.

> A $324,000 property acquisition in the Gordondale/Valhalla area was closed during 2001, expanding our base in the Peace River Arch; and

> a $269,000 acquisition in the Medicine Hat area which augmented our lands and infrastructure.

Exploration and Development

Cigar enjoyed considerable exploration and development success during 2001.

> At *Brazeau, Alberta* – participation in a deep exploratory well resulted in a Nisku gas discovery. Cigar paid 15% of costs and owns a 23.75% interest in the gas well;

> At *Valhalla/Rycroft, Alberta* – Cigar, as operator, drilled and completed two Bluesky gas wells on it's lands retaining between 50% – 60% interest in the wells. Both wells are now on production;

> At *Rainbow, Alberta* – Cigar participated in the drilling of one Keg River gas well and the re-entry of another Keg River gas well on the Company's bank edge play. Both wells were successful and brought on stream in the spring of 2001. Cigar participated for a 25% interest in both wells. The Company also participated in a Keg River re-completion (33% interest), a Slave Point gas recompletion (13.5% interest) and a short radius horizontal Keg River oil well (7% interest). All operations were successful and the wells placed on production;

> At *Hercules, Alberta* – Cigar drilled a 100% interest Viking gas well, placing it on production in June 2001;

> At *Basset Lake, Alberta* – The Company completed a shallow gas well on it's 50% interest land block confirming sufficient reserves to justify a development program for next winter; and

> At *Medicine Hat, Alberta* – The Company completed a 6 well, multi-zone shallow gas drilling program on its 100% owned lands. Three of the wells have now been placed on production.

EQUITY

Cigar issued 340,000 shares by way of a private placement to a new officer of the Company for proceeds of $136,000 in March 2001.

The Company entered into a brokered private placement in June 2001 whereby Cigar issued 1,500,000 common shares priced at $0.75 for net proceeds of $1,024,000. As part of the private placement the Company also issued 850,000 warrants which are convertible into 850,000 common shares at $1.00 per share until June 2002.

It is important to note that Cigar's officers and directors retain a high level of ownership in the Company. Approximately 38% of the basic common shares outstanding are held by management and directors. This ensures that our interests are aligned with those of all shareholders and attests to our personal commitment to, and vested interest in, the creation and enhancement of value for all shareholders.

STRENGTHENED MANAGEMENT

Cigar made two additions to its management team during fiscal 2001.

Mr. James Young, P. Geol. was appointed to the position of Vice President, Exploration in February, responsible for directing the Company's exploration and development activities. Mr. Young has over 27 years of experience with small and intermediate companies in the Industry.

Also in February, Cigar appointed Mr. Roger Boscher as Controller for the Company. Mr. Boscher is a Chartered Accountant with over 12 years of oil and gas experience, formerly acted in a consulting capacity for the Company and is responsible for managing Cigar's financial activities.

BOARD GOVERNANCE

In addition to the Audit Committee, and to ensure that the Company's operations and reporting functions are properly reviewed by independent members of the Board of Directors, Cigar's directors established a Reserve Committee. The Reserve Committee's responsibility is to review and approve the Company's Annual Reserve Report which is prepared by independent engineers. Both the Reserve and Audit Committees have direct channels of communication with the independent engineers and auditors to discuss the quality of the principles applied in the Company's reporting.

INDUSTRY ENVIRONMENT

Strong commodity prices particularly natural gas resulted in record levels of activity as companies reinvested their cash flows.

Consolidation within the industry continued at a rapid pace during the past year with over thirty Canadian oil and gas exploration and development companies being acquired. The majority of these companies were small to intermediate companies which were purchased by larger domestic companies, Royalty Trusts and American based independents. This trend should continue as long as the oil and gas industry values reserves and production higher than stock market valuations.

Activity levels in the industry will continue to track commodity prices.

COMMODITY PRICES

The price of natural gas was very volatile throughout the past fiscal year. Canadian natural gas prices were stable during the summer of 2000 averaging $5 per Mcf but started to gain strength in the fall averaging $7 per Mcf. During the winter when strong demand created by cold weather throughout North America, the capacity of both storage reservoirs and transportation systems to deliver sufficient volumes to meet demand was tested. Record high prices were the result with the price of natural gas averaging $13.50 per Mcf in January.

High natural gas prices resulted in a record level of drilling activity in the Western Canadian Sedimentary Basin the past two years which has resulted in a near term surplus for natural gas. This increased production combined with strong storage injections in the U.S. and Canada and conservation by consumers have resulted in weaker prices.

Prices are expected to recover during 2002 as producers scale back their activity levels, production decline rates remain high and demand continues to grow.

Crude prices were relatively stable throughout the year. The price of crude oil began the fiscal year averaging U.S.$29.72 per Bbl in July and ended the fiscal year at U.S. $27.58 per Bbl in June. OPEC has been able to maintain a supply/demand balance that has kept crude oil trading in a fairly narrow range. The continued strength of crude oil will continue to be determined largely by OPEC's discipline in maintaining a balance between supply and demand and the relative strength of the world economies.

STRATEGY

Cigar shall continue to employ the strategies that have created the success to date. The Company has a motivated team of professionals dedicated to the Company's business plan and focused on sustainable long-term growth and profitability for our shareholders.

Our strategy for growth is based on the following fundamentals:

> build a skilled and experienced team;

> expand activities within core areas;

> balance expenditures between acquisitions and exploration and development;

> maintain balance sheet strength with debt to running cash flow levels of not more than two times;

> concentrate on efficient activities to maximize netbacks;

> generate and operate projects; and

> focus on natural gas and light oil opportunities.

OUTLOOK

The Company achieved record levels of growth last year by maintaining its disciplined approach to its business plan. We strengthened our management team and will continue to build upon our team with experienced and dedicated people.

The Company expanded its ownership of properties within its core growth areas concentrating on areas that provided the Company with year round access, multi-zone potential and good facility infrastructure.

Having established several core areas we will focus the majority of our efforts over the next year in developing the inventory of projects that we have generated within these areas. We continued to mitigate a portion of our risk by bringing in industry partners into our internally generated drilling prospects while still maintaining a large interest and operational control of the projects.

Cigar's exploration and development activities will be funded from the Company's cash flow. We will utilize our expanded line of credit primarily to pursue strategic opportunities and fund facilities.

Cigar is well positioned to continue its strong growth during 2002 and beyond. We will rely upon our experienced dedicated staff, excellent prospect inventory and strong balance sheet to expand and achieve above average results.

We wish to thank our shareholders for their continued support as we continue to expand following our business plan, our Board of Directors for their continued guidance and our staff for their dedication.

For and on behalf of the Board of Directors,

Brian H. Gore
President, Chief Executive Officer
and Chairman of the Board

September 10, 2001

Summary of operations

The Company has now positioned itself within several core areas in which we have built a stable production base and an inventory of new projects. These projects provide the Company with significant growth opportunities as we continue to execute our business plan.

THE ASSET BASE

Cigar's properties and activities are located in 5 focus areas of the Western Canadian Sedimentary Basin in Alberta. These areas comprise a balanced portfolio of producing properties and exploration and development opportunities offering substantial upside potential.

AREA RESERVES, UNDEVELOPED LAND AND PRODUCTION SUMMARY

The following table summarizes Cigar's area land holdings, production and reserves as at June 30, for the 2001 and 2000 fiscal years.

	2001				2000			
	Reserves				Reserves			
Area	Proven & Probable (1) Mboe	Present Value Before Tax Discounted at 10% $ 000's	Undeveloped Lands Net Acres	Average Daily Production June, 2001 Boe/d	Proven & Probable (1) Mboe	Present Value Before Tax Discounted at 10% $ 000's	Undeveloped Lands Net Acres	Average Daily Production June, 2000 Boe/d
Peace River Arch	759	$ 9,649	1,808	215	266	$ 2,345	1,694	42
Rainbow Lake	400	$ 5,149	9,529	168	206	$ 2,311	2,323	62
Hercules	269	$ 3,205	640	84	277	$ 2,825	2,560	125
Brazeau	158	$ 2,095	304	–	–	$ –	–	–
Medicine Hat	142	$ 1,126	7,153	38	–	$ –	–	11
Other	30	$ 240	4,569	14	69	$ 391	6,579	16
ARTC	–	$ 1,314	–	–	–	$ 351	–	–
	1,758	$ 22,778	24,003	519	818	$ 8,223	13,156	256

(1) Probable reserves have been discounted by a factor of 50% to account for the risk associated with such reserves.

DRILLING ACTIVITY

During fiscal 2001, Cigar conducted an active program that included the drilling of 15 gross (9.4 net) wells, the majority of which it operated. The Company retained an average 63% working interest in the wells drilled, achieving an overall success rate of 87%.

The following table, which is illustrative of Cigar's transition to a more active exploration and development company, summarizes the Company's drilling activities during the three fiscal years ending June 30, 2001.

	2001		2000		1999	
wells	**Gross**	**Net**	Gross	Net	Gross	Net
Gas	**11.0**	**7.0**	2.0	0.7	1.0	0.2
Oil	**2.0**	**0.4**	1.0	0.5	–	–
Abandoned	**2.0**	**2.0**	3.0	1.6	–	–
Total	**15.0**	**9.4**	6.0	2.8	1.0	0.2
Success rate	**87%**		50%		100%	
Average working interest	**63%**		47%		20%	

(1) Gross wells are the total number of wells in which Cigar participated.
(2) Net wells reflect the percentage working interest held by Cigar in each of the gross wells.

UNDEVELOPED LAND

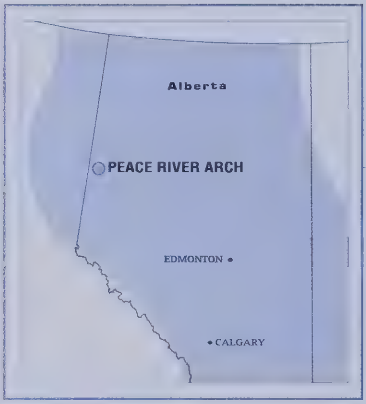
At June 30, 2001 Cigar owned 24,003 net acres of undeveloped land, 80% of which are located within its primary areas of activity. At June 30, 2001, an internal evaluation has attributed a value of $1,427,000 to the Company's undeveloped land inventory.

Land Holdings (at June 30,2001)

	Undeveloped		Developed		Total	
acres	Gross	Net	Gross	Net	Gross	Net
Peace River Arch	7,840	1,808	8,966	2,186	16,806	3,994
Rainbow	20,517	9,529	8,768	867	29,285	10,396
Hercules	640	640	2,560	2,560	3,200	3,200
Brazeau	1,280	304	640	152	1,920	456
Medicine Hat	9,441	7,153	7,520	3,316	16,961	10,469
Other	13,516	4,569	13,941	5,971	27,457	10,540
Total	53,234	24,003	42,395	15,052	95,629	39,055

(1) Gross acres are the total number of acres in which Cigar has an interest.
(2) Net acres reflect Cigar's working interest in the gross acres.

Property & Activity Review



PEACE RIVER ARCH

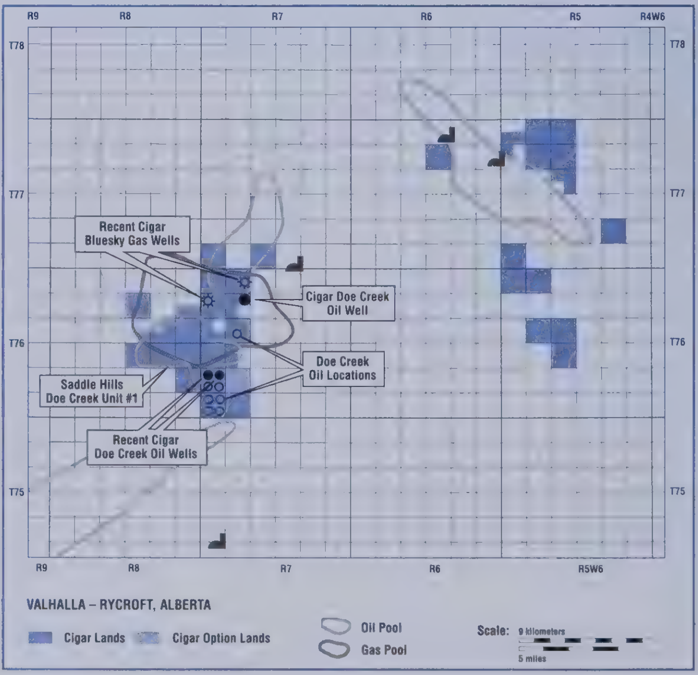
Cigar holds varying working and royalty interests in a total of 16,806 acres of land in the PRA. This area accounted for:

> 35% of production volumes last year;

> 43% of reserves at year end 2001;

> 8% of undeveloped land holdings at year end 2001.

The Peace River Arch ("PRA") has become a major focus area for Cigar. This region of Northwest Alberta is known for its prolific, high deliverability oil and gas reservoirs located in multiple horizons ranging in depth from the Doe Creek at about 600 metres to the Kiskatinaw and Wabamun horizons which occur at approximately 2,300-3,100 metres. The PRA is serviced by an excellent transportation and facilities infrastructure, enabling new discoveries to be brought onstream within a reasonably short timeframe.



Cigar acquired its initial position in the **Valhalla/Rycroft Area** through the acquisition of Pivotal Energy, which was acquired effective January 2, 2000.

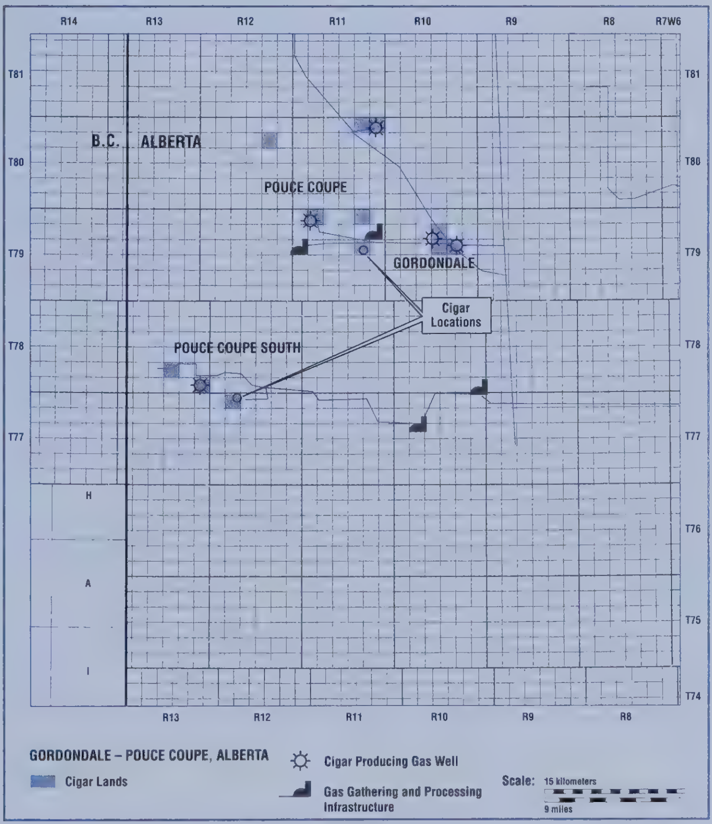
The Company drilled two Bluesky gas wells during the year. The 8-32-76-7W6M (Cigar 50% interest) is producing 300 Mcfd. The 12-30-76-7W6m (Cigar 59% interest) is producing 600 Mcfd.

An active Doe Creek light oil development program (Cigar 47% interest) has recently commenced. This shallow development will involve the drilling of up to 10 wells.

The Company established its presence in the **Gordondale/Pouce Coupe Area** of the PRA through a $324,000 property acquisition on March 30, 2001.

A workover on the Cigar operated 3-32-79-11W6M well (Cigar 50% interest) resulted in a production increase of 500 Mcfd from the well.

Additional gas prospects have been identified and are scheduled for drilling this fall.

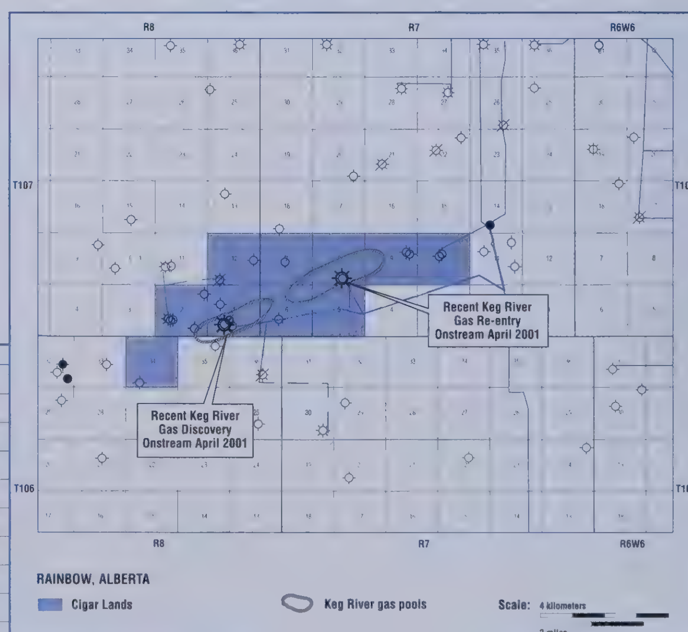


RAINBOW LAKE AREA, NW Alberta

Cigar holds varying working and royalty interests in a total of 29,285 acres of land between Townships 104 to 121 and Ranges 4 to 9 west of the sixth meridian. This area accounted for:

> 29% of production volumes last year;
> 23% of reserves at year end 2001; and
> 40% of undeveloped land holdings at June 30, 2001.

The Rainbow Lake Area of northwest Alberta is characterized by prolific reservoirs located in shallow to medium depth horizons. The area is recognized for oil and gas production from the Keg River, Sulphur Point and Slave Point formations as well as shallow gas from the Bluesky formation.



During the year, the Company participated in two Keg River bank edge wells. The 2-8-107-8 W6M recompletion (Cigar 23% interest) tested at 2.6 mmcfd and 120 bbls per day of condensate. The 7-1-107-8 W6M (Cigar 25% interest) tested at 2.0 MMcfd and 84 bbls per day of condensate. Both wells were tied-in to a gathering system and commenced production in April, 2001.

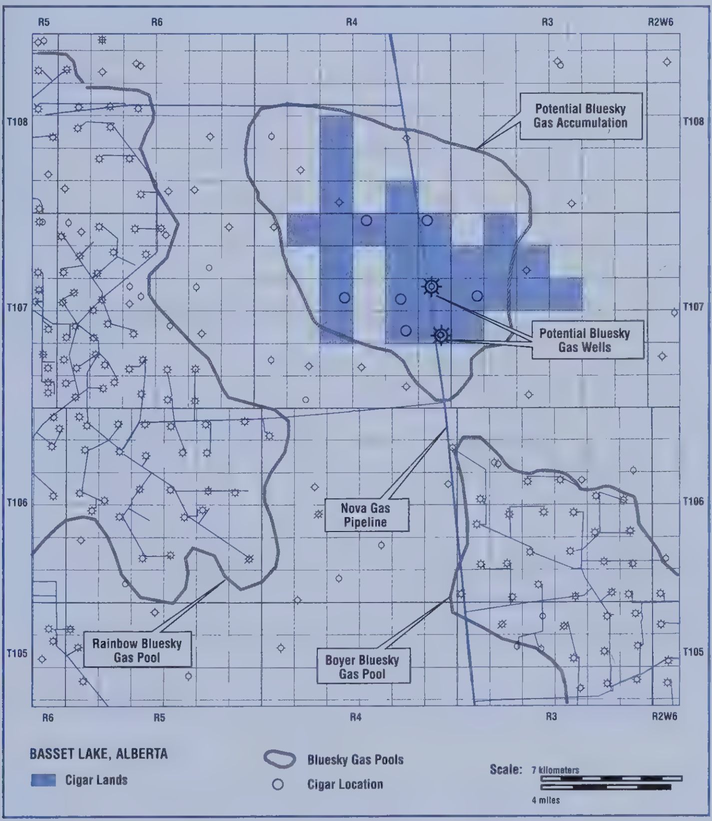
Remedial work on the 11-10-107 7W6M (Cigar 50% interest) well drilled in 2000 was unsuccessful and the Keg River was abandoned.

A Keg River short radius horizontal re-entry at a suspended Keg River oil well located at 6-27-114-6 W6M (Cigar 7.1% interest) is currently producing 150 bbls per day.

Another Keg River recompletion at 6-13-119-7 W6M (Cigar 32.7% interest) commenced production in April, 2001 at a restricted rate. With the access and facility capacity constraints now alleviated, this well is currently producing at a daily rate of 1.0 MMcf of gas and 130 bbls of oil.

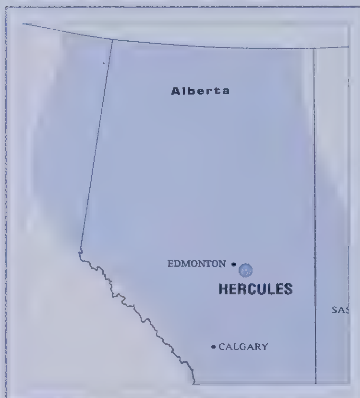
An uphole Slave Point gas recompletion of a suspended Keg River oil well located at 1-36-114-7 W6M (Cigar 18.4% interest) commenced production at 300 Mcf per day in June, 2001.

Additional re-entries and recompletions are planned for next winter on Cigar interest lands.



Cigar completed its first well on its 50% interest Basset Lake lands during March 2001. Flow rates from this Bluesky gas well support a multi-well shallow gas development project. The Company has now assembled 17,280 gross acres (8,640) net acres at Basset Lake and plans additional drilling during the 2001-2002 winter drilling season.

The Basset Lake property is located adjacent to a Nova gas transportation line and being dry, sweet gas, requires only dehydration and compression to bring the gas to market.

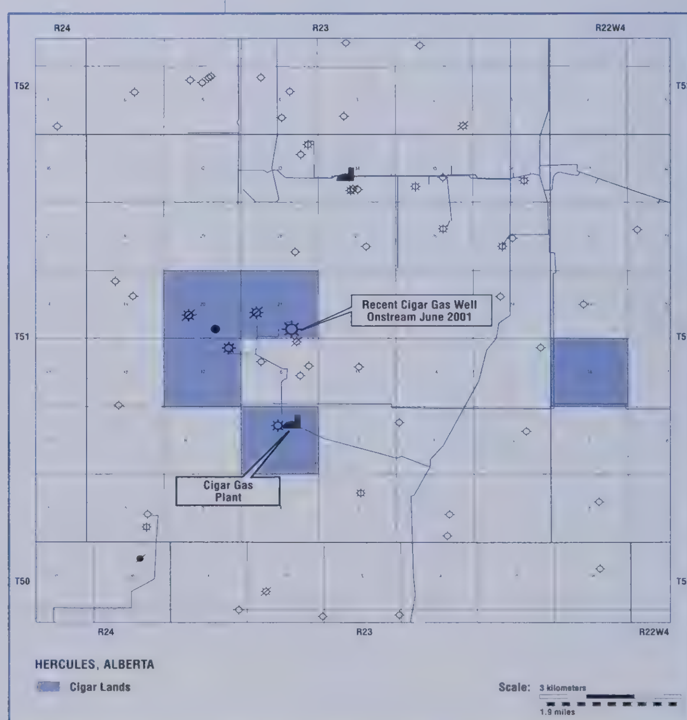


HERCULES AREA, Alberta

Cigar holds a 100% interest in 3,200 acres of land and owns a 100% interest in a compressor station and gas gathering system. The property accounted for:

- 25% of production volumes last year;
- 15% of reserves at fiscal year end 2001;
- 3% of undeveloped land holdings at June 30, 2001.

The Hercules Property is located in central Alberta approximately 20 miles southeast from Edmonton. The area is mainly prospective for shallow gas in the Belly River, Viking and Mannville sands.



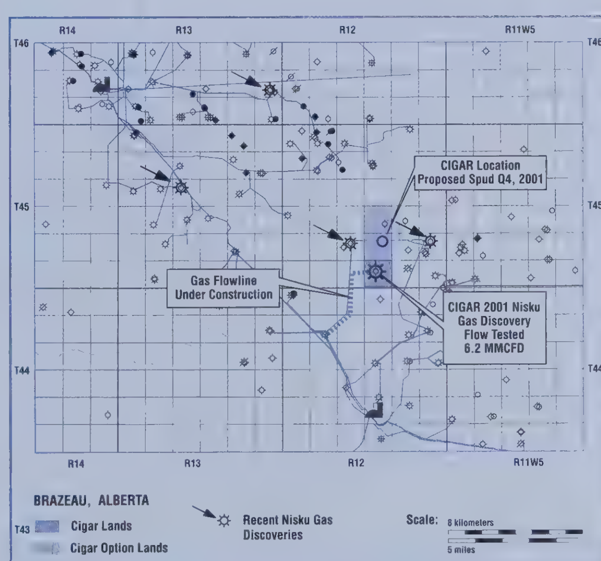
During the year, the Company completed and tied-in a 100% interest Viking gas well, 2-21-51-23W4M in conjunction with the installation of a new compressor to increase production to 800 Mcfd. The evaluation of additional opportunities in the area is ongoing. Any new wells drilled by Cigar can be placed on production through our controlled existing infrastructure.

BRAZEAU AREA, Alberta

The Company's deepest well to date was drilled in the Brazeau Area of west central Alberta, approximately 90 miles southwest of Edmonton.

During early 2001, the Brazeau 11-3-45-12W5M (Cigar 23.75% interest) 3,400 meter exploratory well was drilled and completed as a Nisku Reef gas well. The well was flow tested at a restricted rate of 6.2 MMcfd at a flowing tubing head pressure of 4,083 psig and will be tied into the area's infrastructure during the month of November 2001. Anticipated production rates from the well are expected to be approximately 6-8 MMcfd with associated natural gas liquids.

The Company has an option to earn a 23.75% interest in a similar geophysical anomaly on offsetting lands and anticipates that a second well will be drilled late in the calendar year.



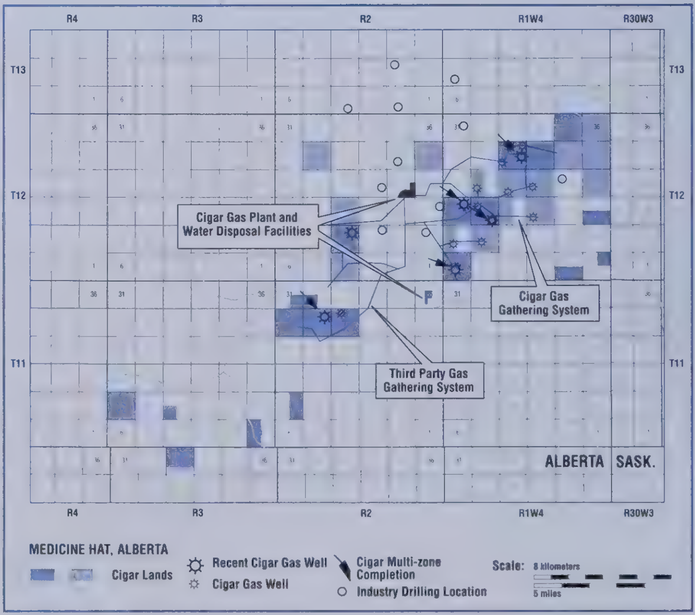
MEDICINE HAT AREA, Alberta

Cigar holds an average 62% interest in 16,961 acres of land. This property represents:

> 7% of production volumes last year;
> 8% of Company's reserves at year end 2001;
> 30% of Cigar's undeveloped land holdings at year end 2001.

This shallow gas prone area is known for its long life, low deliverability gas reserves from the Milk River, Medicine Hat and Second White Specks sands.

During the year, Cigar acquired and reactivated a 10 well project (80% average interest) along with a compressor station, gathering system and water disposal well. The Company drilled an initial six well (100% interest) program to further evaluate the gas potential in the area. Initial completion results are encouraging and three of the wells have been placed on production.



PETROLEUM AND NATURAL GAS RESERVES

Escalated prices and costs at at June 30, 2001

In their report dated July 13, 2001, ("the GLJ Evaluation"), Gilbert Lausten Jung Associates Ltd. ("GLJ") have evaluated Cigar's petroleum and natural gas reserves as at June 30, 2001. The following table summarizes the volumes and present value of the Company's reserves:

	Natural Gas		Oil and NGL's		Present Value Of Cash Flow ($000's) Before Tax Discounted At		
	Gross (mmcf)	Net (mmcf)	Gross (mbbls)	Net (mbbls)	0%	10%	15%
Proven							
Producing	4,052	3,170	210	168	$ 15,101	$ 11,775	$ 10,723
Non-producing	3,010	2,310	25	18	$ 8,157	$ 6,521	$ 5,927
Total Proven	7,062	5,480	235	186	$ 23,258	$ 18,296	$ 16,650
Probable [1]	1,805	1,440	45	35	$ 5,081	$ 3,161	$ 2,626
ARTC	–	–	–	–	$ 1,655	$ 1,321	$ 1,207
Total	8,867	6,920	280	221	$ 29,994	$ 22,778	$ 20,483

(1) Probable reserves have been discounted by a factor of 50% to account for the risk associated with such reserves.

(2) Gross reserves are the total remaining recoverable reserves owned by Cigar before deduction of royalties. Net reserves are defined as those accruing to Cigar after deduction of royalties.

(3) The price forecast used in determining the value of cash flow is based on the July 1, 2001 GLJ price forecast.

RECONCILIATION OF RESERVES

The following table details the changes in gross reserves since June 30, 1999:

	Natural Gas (mmcf)			Oil and NGL's (mbbls)			Boe (mboe @ 6:1)		
	Proven	Probable [1]	Total	Proven	Probable [1]	Total	Proven	Probable [1]	Total
June 30, 1999	57.0	25.0	82.0	96.0	37.0	133.0	105.5	41.2	146.7
Discoveries	723.0	207.0	930.0	11.0	42.0	53.0	131.5	76.5	208.0
Acquisitions	2,145.0	302.0	2,447.0	78.0	9.0	87.0	435.5	59.3	494.8
Production	(165.0)	0.0	(165.0)	(33.0)	0.0	(33.0)	(60.5)	0.0	(60.5)
Dispositions	(450.0)	0.0	(450.0)	0.0	0.0	0.0	(75.0)	0.0	(75.0)
Revisions to prior estimates	548.0	21.0	569.0	22.0	(13.0)	9.0	113.3	(9.5)	103.8
June 30, 2000	2,858.0	555.0	3,413.0	174.0	75.0	249.0	650.3	167.5	817.8
Discoveries	2,736.7	712.2	3,448.9	65.6	0.9	66.5	521.8	119.5	641.3
Acquisitions	2,019.2	591.3	2,610.5	32.4	5.1	37.5	368.9	103.7	472.6
Production	(551.9)	0.0	(551.9)	(37.0)	0.0	(37.0)	(129.0)	0.0	(129.0)
Dispositions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Revisions to prior estimates	0.0	(53.5)	(53.5)	0.0	(36.0)	(36.0)	0.0	(44.9)	(44.9)
June 30, 2001	**7,062.0**	**1,805.0**	**8,867.0**	**235.0**	**45.0**	**280.0**	**1,412.0**	**345.8**	**1,757.8**

(1) Probable reserves have been discounted by a factor of 50% to account for the risk associated with such reserves.

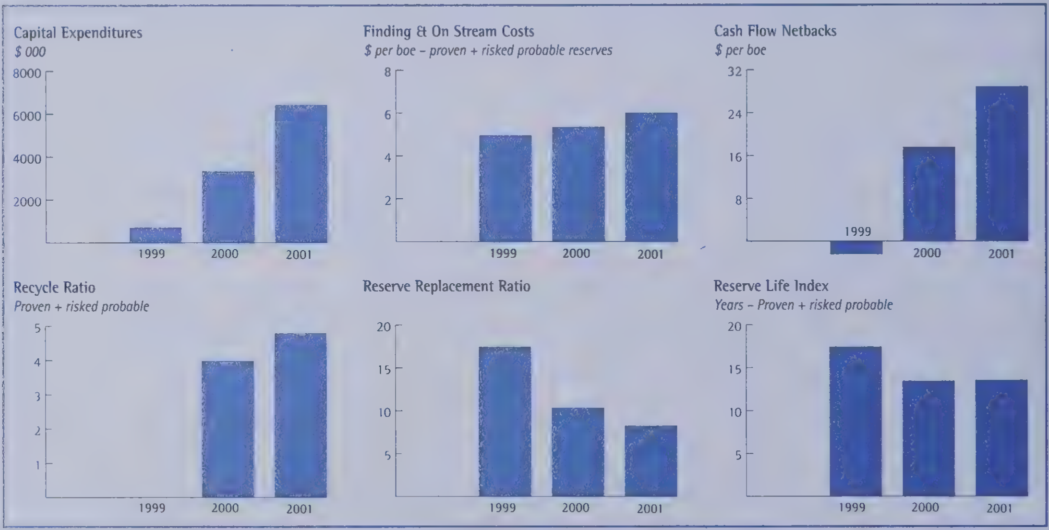
PERFORMANCE MEASURES

During fiscal 2001, Cigar incurred capital expenditures of $6,448,724 (2000 – $3,367,364) and added proved and risked probable reserves of 1,069,000 boe (2000 – 627,600 boe) at a cost of $7.24 per boe (proven) and $6.03 per boe (proven plus risked probable) reserves. The Company's Finding and On Stream Costs for reserve additions place us in the upper quartile of our peer group.

Cigar's Cash Flow Netback per boe was 4.0 (proven) and 4.8 (proven plus risked probable) times greater than the cost of finding or replacing a boe. This Reserve Recycle ratio is in the upper quartile of our peer group.

Stated on a boe basis, the Company's Reserve Replacement Ratio in fiscal 2001 was 6.9 (proven) and 8.3 (proven plus risked probable) times Cigar's production volume for the year.

With a bias toward natural gas, and a Reserve Life Index of 10.9 (proven) and 13.6 (proven plus risked probable) years, Cigar is well positioned to benefit from future increases in natural gas prices and demand.



	2001	% change	2000	% change	1999
Capital expenditures	$ 6,448,724	92%	$ 3,367,364	359%	$ 733,437
Reserves added (mboe)					
Proven	890.7	81%	492.8	366%	105.8
Proven plus risked probable	1,069.0	70%	627.6	326%	147.2
Finding and onstream costs ($/boe)					
Proven	$ 7.24	6%	$ 6.83	(1%)	$ 6.93
Proven plus risked probable	$ 6.03	12%	$ 5.37	8%	$ 4.98
Cash flow netback	$ 28.97	64%	$ 17.66	–	$ (2.38)
Reserve recycle ratio (cash flow netback/finding and onstream costs)					
Proven	4.0	54%	2.6	–	$ –
Proven plus risked probable	4.8	45%	3.3	–	$ –
Production volumes (mboe)	129.0	114%	60.4	619%	8.4
Reserve replacement ratio (reserve additions/production)					
Proven	6.9	(16%)	8.2	(35%)	12.6
Proven plus risked probable	8.3	(20%)	10.4	(41%)	17.5
Reserves (mboe)					
Proven	1,412	117%	650	513%	106
Proven plus risked probable	1,758	115%	818	456%	147
Reserve life index (years)					
Proven	10.9	1%	10.8	(14%)	12.6
Proven plus risked probable	13.6	1%	13.5	(23%)	17.5

Summary of our Accounts

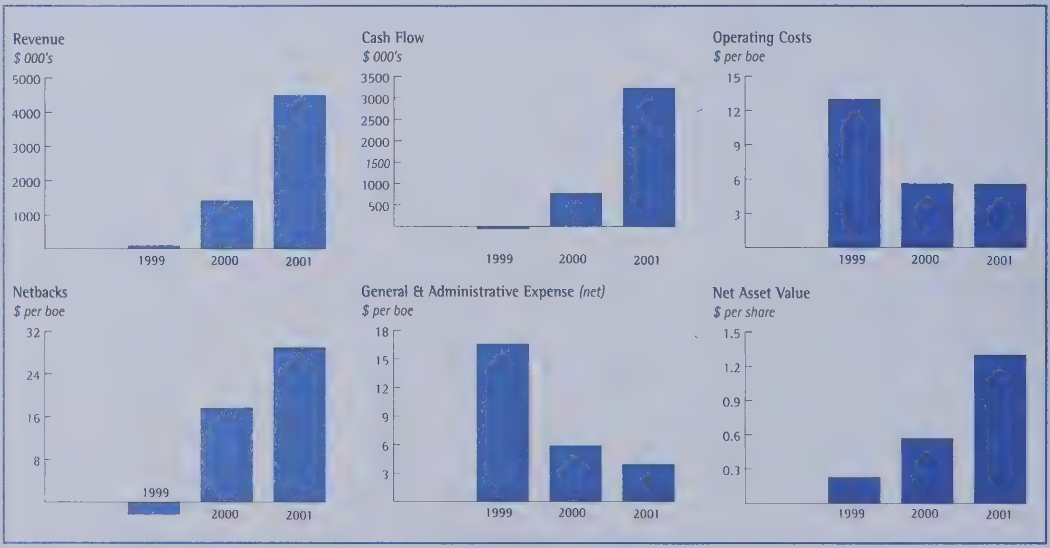
Fiscal 2001 produced record setting results for Cigar as cash flow from operations and net income increased 314% and 193% respectively over fiscal 2000. Production volumes per boe increased 114% while commodity prices increased by 48% per boe over last year.

Management's Discussion & Analysis of Financial Condition & Results of Operations

The following discussion and analysis of financial results should be read in conjunction with the financial statements for the years ended June 30, 2001 and 2000.

Where amounts are expressed on a barrel of oil equivalent (Boe) basis, natural gas volumes have been converted to barrels of oil equivalent at six thousand cubic feet per barrel of oil equivalent. This conversion rate approximates the relative energy content between natural gas and oil.

FINANCIAL HIGHLIGHTS



ANALYSIS OF RESULTS OF OPERATIONS

Overview

Fiscal 2001 produced record setting results for Cigar as cash flow from operations and net income increased 314% and 193% respectively over fiscal 2000. Production volumes per boe increased 114% while commodity prices increased by 48% per boe over last year.

Petroleum and natural gas revenues

Petroleum and natural gas revenue increased to $5.7 million in fiscal 2001, a 214% increase from $1.8 million in fiscal 2000 due to increased production volumes and the strength of commodity prices. The following table shows the components of revenue by product.

	2001	% change	2000	% change	1999
Petroleum and NGL's	$ 1,573,211	32	$ 1,187,868	–	–
Natural gas	$ 4,086,499	570	$ 609,486	450	$ 110,762
Royalty and miscellaneous	$ 44,298	104	$ 21,665	21	$ 17,957
Total petroleum and natural gas revenue	$ 5,704,008	214	$ 1,819,019	1,313	$ 128,719

The following table shows the components of revenue for fiscal 2001 and 2000 indicating the effects of changes in production volumes and commodity prices.

	Petroleum & NGL	Natural Gas	Other	Total
Fiscal 2000 revenue	$ 1,187,868	$ 609,486	$ 21,665	$ 1,819,019
Effect of increase in production	$ 150,654	$ 1,421,636	–	$ 1,572,290
Effect of increase in commodity price	$ 234,689	$ 2,055,377	–	$ 2,290,066
Other	–	–	$ 22,633	$ 22,633
Fiscal 2001 revenue	$ 1,573,211	$ 4,086,499	$ 44,298	$ 5,704,008

Production volumes

The Company continued to increase it production base in 2001 achieving a 12% growth in daily production of light petroleum and natural gas liquids. The Company's bias toward natural gas has resulted in a 235% increase in daily production of natural gas. On a boe basis, the Company averaged an increase of 114% increase in daily production. Cigar exited the year with daily production of 500 boe per day.

	2001	% change	2000	% change	1999
Petroleum and NGL's (Bbl)					
Total	36,995	13	32,832	–	–
Per day	101	12	90	–	–
Natural gas (Mcf)					
Total	551,856	233	165,542	229	50,370
Per day	1,512	235	452	228	138
Boe at 6:1 (Boe)					
Total	128,971	113	60,422	620	8,395
Per day	353	114	165	617	23

Commodity prices

Commodity prices remained strong throughout the year. Petroleum and NGL prices averaged $42.52 per barrel and natural gas prices averaged $7.41 per mcf, an increase of 18% and 101% as compared to 2000.

	2001	% change	2000	% change	1999
Petroleum and NGL's (per bbl)	$ 42.52	18	$ 36.18	–	–
Natural gas (per mcf)	$ 7.41	101	$ 3.68	67	$ 2.20
Per Boe	$ 43.88	48	$ 29.74	125	$ 13.19

Royalties

Petroleum and natural gas royalties, net of ARTC, increased to $1.2 million in fiscal 2001, a 208% increase from $390,554 in 2000 as a result of higher production volumes and commodity prices. Net royalties per Boe increased to $9.34 per boe from $6.46 per boe, a 45% increase as a result of increased commodity prices rising 48% per boe. Royalties as a percentage of revenue remained constant at just over 21%.

	2001	% change	2000	% change	1999
Crown	$ 930,794	159	$ 359,695	44,806	$ 801
Freehold and overriding	$ 323,026	833	$ 34,609	66	$ 20,831
Total royalties	$ 1,253,820	218	$ 394,304	1,723	$ 21,632
ARTC	$ (49,539)	1,221	$ (3,750)	–	$ –
Net royalties	$ 1,204,281	208	$ 390,554	1,705	$ 21,632
Per Boe	$ 9.34	45	$ 6.46	150	$ 2.58
As a percent of sale price per boe	21.3%	(2)	21.7%	11	19.6%

Operating costs

Operating costs increased to $719,398 in fiscal 2001, a 112% increase from $339,640 in 2000 as a result of increased production volumes. On a per unit basis, operating costs were virtually unchanged from the prior year. General operating cost increases were offset by productivity gains achieved through focused production in core areas.

	2001	% change	2000	% change	1999
Petroleum and NGL's	$ 211,491	15	$ 184,552	–	$ –
Natural gas	$ 507,907	227	$ 155,088	42	$ 109,102
Total production costs	$ 719,398	112	$ 339,640	211	$ 109,102
Per barrel of petroleum	$ 5.72	2	$ 5.62	–	$ –
Per mcf of natural gas	$ 0.92	(2)	$ 0.94	(57)	$ 2.17
Per barrel of oil equivalent	$ 5.58	(1)	$ 5.62	(57)	$ 13.00

Netbacks

	2001	% change	2000	% change	1999
Petroleum and NGL's					
Sales price per bbl	$ 42.52	18	$ 36.18	–	–
Crown royalties	$ (8.44)	(2)	$ (8.60)	–	–
Freehold and overriding	$ (0.23)	–	$ –	–	–
ARTC	$ 0.14	367	$ 0.03	–	–
Production costs	$ (5.72)	2	$ (5.62)	–	–
Netback per bbl	$ 28.27	29	$ 21.99	–	–
Natural gas					
Sales price per mcf	$ 7.41	101	$ 3.68	67	$ 2.20
Crown royalties	$ (1.12)	138	$ (0.47)	–	$ (0.02)
Freehold and overriding	$ (0.57)	171	$ (0.21)	(49)	$ (0.41)
ARTC	$ 0.08	300	$ 0.02	–	$ –
Production costs	$ (0.92)	(2)	$ (0.94)	(57)	$ (2.17)
Netback per mcf	$ 4.88	135	$ 2.08	–	$ (0.40)
Boe (6:1)					
Sales price per boe	$ 43.88	48	$ 29.74	125	$ 13.19
Crown royalties	$ (7.22)	21	$ (5.95)	6,511	$ (0.09)
Freehold and overriding	$ (2.49)	337	$ (0.57)	(77)	$ (2.48)
ARTC	$ 0.38	533	$ 0.06	–	$ –
Production costs	$ (5.58)	(1)	$ (5.62)	(57)	$ (13.00)
Netback per boe	$ 28.97	64	$ 17.66	–	$ (2.38)

General and administrative expenses

General and administrative expense in 2001 increased to a gross $736,000 compared to $517,000 for 2000. The increase of 42% over 2000 can be attributed mainly to the hiring of additional personnel and general increases in costs as a result of increase activity undertaken in 2001. On a boe basis, general and administrative expense was $3.96 in 2001, a decrease of 33% from $5.91 in 2000. The per unit decrease is attributed to Cigar's successful effort to increase Cigar's 2001 average production volume to 353 boe per day in 2001 from 165 boe per day in 2000.

	2001	% change	2000	% change	1999
Gross	$ 736,603	42	$ 516,954	271	$ 139,390
Capitalized	$ (225,748)	41	$ (159,800)	–	$ –
Net	$ 510,855	43	$ 357,154	156	$ 139,390
Gross per boe	$ 5.71	(33)	$ 8.55	(48)	$ 16.60
Capitalized per boe	$ (1.75)	(34)	$ (2.64)	–	$ –
Net per boe	$ 3.96	(33)	$ 5.91	(64)	$ 16.60

Interest expense

The Company incurred interest expense of $37,500 during the year resulting from utilizing the demand loan facility and financing the unspent portion of the flow-through share renunciations on shares issued in December 1999.

Depletion, depreciation and site restoration

Depletion is provided for on a unit of production based on total proven reserves. As a result higher finding and on-stream costs, the Company's rate for providing of petroleum and natural gas assets in fiscal 2001 increased to $6.17 per boe, an increase of 70% over $3.64 per boe in 2000.

	2001	% change	2000	% change	1999
Petroleum and natural gas	$ 796,370	262	$ 219,765	4,327	$ 4,964
Facilities and other assets	$ 109,766	191	$ 37,758	–	$ 40
Provision for site restoration	$ 36,955	(24)	$ 48,610	235	$ 14,500
Total	$ 943,091	208	$ 306,133	1,470	$ 19,504
Per boe (6:1)					
Petroleum and natural gas	$ 6.17	70	$ 3.64	517	$ 0.59
Facilities and other assets	$ 0.85	35	$ 0.63	–	$ –
Provision for site restoration	$ 0.29	(64)	$ 0.80	(54)	$ 1.73
Total per boe	$ 7.31	44	$ 5.07	118	$ 2.32

Future income taxes

Future income taxes of $902,000 was recorded in 2001 as compared to nil in 2000. The Company adopted the new Canadian Institute of Chartered Accountants recommendation to account for future income taxes based on the liability method effective July 1, 2000. The new method was applied retroactively without restatement of the 2000 financial statements. As a result, the future income tax liability increased by $1.042 million, capital assets increased by $653,000 and retained earnings decreased by $389,000. As a result of the change, the effect on net income for 2001 was a reduction of $46,000, with no effect on earnings per share.

As at June 30, 2001, the Company has $4,800,000 in available income tax pools to offset the payment of current income taxes on future taxable income and is comprised of:

Undepreciated Capital Cost (UCC)	$ 1,431,000
Canadian Oil & Gas Property Expense (COGPE)	$ 1,084,000
Canadian Development Expense (CDE)	$ 1,513,000
Canadian Exploration Expense (CEE)	$ 684,000
Other	$ 88,000
Total	$ 4,800,000

Capital expenditures

During fiscal year 2001, the Company's net capital expenditures were $6,448,700 as compared to $3,367,400 in 2000. These expenditures added 890,700 of boe's to the Company's proven reserves, resulting in a reserve replacement ratio of 6.9 times. The following summarizes these expenditures by major category:

	2001	2000	1999
Drilling and completions	$ 3,695,700	$ 1,645,700	$ –
Well equipment and facilities	$ 1,212,300	$ 177,100	$ 85,106
Land	$ 753,000	$ 400,400	$ 34,030
Seismic	$ 150,800	$ 65,500	$ –
Other	$ 103,500	$ 71,800	$ 475
Corporate acquisitions	–	$ 1,714,900	$ –
Property acquisition	$ 593,400	–	$ 613,826
Property disposition	$ (60,000)	$ (708,000)	$ –
Total	$ 6,448,700	$ 3,367,400	$ 733,437

The Company added new reserves at a finding and on stream cost of $7.24 per boe ($6.83 in 2000) on a proven basis and $6.03 ($5.37 in 2000) per boe on a proven plus risked probable basis.

LIQUIDITY AND CAPITAL RESOURCES

The Company's liquidity has been greatly enhanced during 2001. Due to higher production volumes and strong commodity prices the Company realized cash flow from operations of $3.2 million which the Company used to fund over one-half of the capital expenditure program.

In June 2001, the Company completed a private placement of 1,500,000 units at $0.75 per unit for net proceeds of $1.02 million. Each unit consists of one common share and one-half common share purchase warrant. Each full purchase warrant entitles the holder to acquire one common share of the Company at a purchase price of $1.00 per share exercisable on or before June 6, 2002, In addition, 100,000 agent's warrants were issued for the purchase of 100,000 common shares at $1.00 per share exercisable on or before June 6, 2002. If these common share purchase warrants are exercised, the Company would issue 850,000 common shares for proceeds of $850,000.

At June 30, 2001, the Company has 1,200,000 stock options outstanding of which 933,333 were exercisable at an average price of $0.34 equating to proceeds of $316,000.

At June 30, 2001, the Company has a demand credit facility with a Canadian Chartered bank in the amount of $3.0 million, under which the Company has utilized $118,000. The Company has since renegotiated an increase in the demand credit facility to $6.0 million.

At June 30, 2001, the Company has a working capital deficiency of $1.8 million representing a debt to cash flow ratio of 0.56:1. As June 30, 2000, the Company had working capital of $236,000.

The Company intends to fund ongoing exploration, development and acquisition activities from internally generated cash flow, bank debt and the issuance of common shares.

NET ASSET VALUE

The following table summarizes the estimated net asset value of the Company as at June 30, 2001 and 2000 based on an independent reserve evaluation using proven and risked probabale reserves and escalating commodity prices before income taxes discounted at 10%.

	2001	2000	1999
Petroleum and natural gas reserves	$ 22,778,000	$ 8,223,000	$ 1,473,000
Undeveloped land	$ 1,427,000	$ 710,000	$ 46,000
Other assets	–	$ 150,000	$ 150,000
Working capital (deficiency)	$ (1,818,000)	$ 236,000	$ 1,032,000
Total net asset value, basic	$ 22,387,000	$ 9,319,000	$ 2,701,000
Number of share outstanding, basic	17,611,639	15,771,639	12,042,692
Net asset value per share, basic	$ 1.27	$ 0.59	$ 0.22
Options assumed exercised	$ 418,000	$ 372,000	$ 213,000
Warrants assumed exercised	$ 850,000	–	–
Total net asset value, diluted	$ 23,655,000	$ 9,691,000	$ 2,932,000
Number of shares outstanding, diluted	19,661,639	16,871,639	12,692,692
Net asset value per share, diluted	$ 1.20	$ 0.57	$ 0.23

SHARE INFORMATION

The Company's common shares are listed for trading on the Canadian Venture Exchange under the symbol "CGR". At June 30, 2001, the Company had outstanding 17,611,639 common shares, 1,200,000 stock options at an average price of $0.35 and 850,000 common share purchase warrants at a price of $1.00. The Company's market capitalization at June 30, 2001 was $15.9 million.

BUSINESS RISKS

The business of oil and natural gas exploration, development, production and marketing involves many risks and uncertainties. These include the uncertainty of finding new reserves, reservoir performance, commodity price fluctuations, interest rates, the availability of capital to fund continuing exploration and development programs, taxation, regulatory and environmental requirements. The Company manages these risks by employing competent professional staff and consultants, employing sound operating practices utilizing the most advanced technology available and funding the Company's capital expenditure program through the utilization of cash flow from operations together with the prudent issue of equity to ensure that bank indebtedness remains manageable.

Oil and natural gas commodity prices are influenced by continental, worldwide and seasonal supply and demand factors, competitive conditions, availability of transportation, the US dollar exchange rate and political stability. As commodity prices are quoted in US dollars, the fluctuations in the US/Canada exchange rates affects the Company's oil and natural gas revenues. The Company has chosen not to utilize hedging strategies to lessen the impact of these fluctuations as the Company's current oil and natural gas production volumes do not justify such measures.

The industry is subject to extensive government regulation related to the protection of the environment. The Company is committed to meeting its responsibility to protect and preserve the environment and takes a proactive approach on all environmental issues.

Financial Reports

MANAGEMENT'S REPORT TO THE SHAREHOLDERS

The accompanying financial statements and all information in this annual report are the responsibility of management and the Board of Directors of the Company. The financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and include certain estimates that reflect management's best judgments. The financial and operating information presented in the Annual Report is consistent with that shown in the financial statements.

Management maintains an appropriate system of internal controls, which ensure transactions are appropriately authorized and accurately recorded, assets are safeguarded and financial records are properly maintained.

External auditors, appointed by the shareholders, have conducted an examination of the financial statements and have provided an independent professional opinion. The Audit Committee, appointed by the Board of Directors and comprised of a majority of directors which are not officers or employees of the Company, has reviewed the financial statements with management and the external auditors and has reported to the Board of Directors. The Board has approved the financial statements.

Brian H. Gore
President & Chief Executive Officer

Calgary, Alberta
August 17, 2001

Financial Reports

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the balance sheets of Cigar Oil & Gas Ltd. as at June 30, 2001 and 2000 and the statements of operations and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the company as at June 30, 2001 and 2000 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants
Calgary, Canada

August 17, 2001

Financial Statements

BALANCE SHEET

June 30, 2001 and 2000

		2001	2000
ASSETS			
Current			
Cash		$ –	$ 315,604
Accounts receivable		1,034,162	843,112
Prepaid expenses		86,825	82,505
		1,120,987	1,241,221
Capital assets	*(Note 3)*	9,272,931	3,170,573
		$ 10,393,918	$ 4,411,794
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current			
Bank loan	*(Note 4)*	$ 118,835	$ –
Accounts payable and accrued liabilities		2,819,856	1,005,593
		2,938,691	1,005,593
Provision for site restoration		5,792	61,928
Future income taxes	*(Note 5)*	1,900,402	–
		4,844,885	1,067,521
Shareholders' equity			
Share capital	*(Note 6)*	4,072,162	2,869,328
Retained earnings		1,476,871	474,945
		5,549,033	3,344,273
		$ 10,393,918	$ 4,411,794

See accompanying notes to the financial statements

Approved on behalf of the Board:

Brian H. Gore
Director

M. H. (Mike) Shaikh
Director

STATEMENT OF OPERATIONS AND RETAINED EARNINGS

For the years ended June 30, 2001 and 2000

		2001	2000
Revenue			
Petroleum and natural gas		$ 5,704,008	$ 1,819,019
Royalties, net of ARTC		(1,204,281)	(390,554)
Interest income		3,734	49,407
		4,503,461	1,477,872
Expenses			
Operating		719,398	339,640
General and administrative		510,855	357,154
Interest		37,481	–
Depletion, depreciation and site restoration		943,091	306,133
		2,210,825	1,002,927
Net income before income taxes		2,292,636	474,945
Future income taxes	*(Note 5)*	901,674	–
Net income		1,390,962	474,945
Retained earnings (deficit), beginning of year		474,945	(8,387,952)
Adjustment to reflect adoption of liability method of accounting for future income taxes	*(Note 5)*	(389,036)	–
Reduction in stated capital	*(Note 6)*	–	(8,387,952)
Retained earnings, end of year		$ 1,476,871	$ 474,945
Net income per share, basic and diluted	*(Note 7)*	$ 0.09	$ 0.03

See accompanying notes to the financial statements

STATEMENT OF CASH FLOWS

For the years ended June 30, 2001 and 2000

		2001	2000
Operating activities			
Net income		$ 1,390,962	$ 474,945
Add items not requiring cash:			
Depletion and depreciation		906,136	257,522
Future site restoration		36,955	48,611
Future income taxes		901,674	–
Cash flow from operations		3,235,727	781,078
Net change in non-cash working capital	*(Note 8)*	(277,474)	(117,591)
Cash provided by operating activities		2,958,253	663,487
Financing activities			
Increase in bank loan		118,835	–
Issuance of share capital, net of expenses of $101,335 (2000 - $3,859)		1,159,665	799,956
Cash provided by financing activities		1,278,500	799,956
Investing activities			
Purchase of capital assets		(6,415,633)	(2,428,765)
Site restoration expenditures		(93,091)	(1,183)
Proceeds on disposition of capital assets		60,000	708,000
Business acquisitions	*(Note 2)*	–	(945,416)
Disposition of investment	*(Note 6)*	–	276,020
Net change in non-cash working capital	*(Note 8)*	1,896,367	211,544
Cash used in investing activities		(4,552,357)	(2,179,800)
Decrease in cash		(315,604)	(716,357)
Cash, beginning of year		315,604	1,031,961
Cash, end of year		$ –	$ 315,604
Cash flow per share, basic and diluted	*(Note 7)*	$ 0.20	$ 0.05

See accompanying notes to the financial statements

Notes to the Financial Statements

Cigar Oil & Gas Ltd. ("Cigar" or the "Company") is engaged in the exploration, development and production of petroleum and natural gas. These financial statements have been prepared in accordance with generally accepted accounting principles in Canada. Management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as at the date of the financial statements and the reported amounts of revenues and expenses during the reported year. Actual results could differ from these estimates.

1. SIGNIFICANT ACCOUNTING POLICIES

(a) Capital assets

The Company accounts for petroleum and natural gas properties in accordance with the Canadian Institute of Chartered Accountants guideline on full cost accounting in the petroleum and natural gas industry, whereby all costs associated with the acquisition, exploration and development of petroleum and natural gas reserves are capitalized.

The Company applies a ceiling test to capitalized costs to ensure that the carrying value does not exceed the estimated future net revenues from production of proven reserves, at prices and operating costs in effect at the balance sheet date, plus the cost of unevaluated properties less future general and administrative expenses, financing costs, estimated future abandonment costs and income taxes.

Depletion is calculated using the unit-of-production method based on estimated proven reserves before royalties. For purposes of this calculation, reserves and production of natural gas are converted into equivalent barrels of petroleum based on relative energy equivalent ratio of six thousand cubic feet of natural gas to one barrel of crude petroleum.

Well equipment, pipelines and related plant equipment are carried at cost and are depreciated at 10% using the declining balance method.

Proceeds from the disposal of petroleum and natural gas properties are applied against capitalized costs with no gain or loss recorded unless such a sale would alter the depletion rate by greater than 20%.

The Company conducts substantially all of its exploration, development and production activities jointly with others. These financial statements reflect only the Company's proportionate interest in such activities.

(b) Future site restoration costs

The provision for estimated future site restoration is provided for over the life of the estimated proved reserves on a unit-of-production method. Costs are based on the Company's estimates considering current regulations, costs, technologies and industry standards. Actual expenditures incurred are charged against the provision for site restoration.

(c) Flow-through shares

The Company has financed a portion of its exploration and development activities through the issue of flow-through shares. Under the terms of the flow-through issues, the income tax attributes of the related expenditure are renounced to the subscribers. To recognize the foregone tax benefits to the Company, the flow-through shares issued are recorded net of the tax benefits renounced to the subscribers.

(d) Income taxes

Effective July 1, 2000, the Company adopted the new Canadian Institute of Chartered Accountants recommendation to account for future income taxes based on the liability method. The new method was applied retroactively without restatement of the 2000 financial statements. Under the liability method, the Company records future income taxes based on the difference between the accounting and income tax value of an asset or liability. Future income tax assets and liabilities are recorded using expected income tax rates to be applied to taxable income in the years in which these differences are expected to be realized.

Prior to the adoption of the new recommendations, income tax expense was recorded using the deferral method of income tax allocation. Deferred income tax expense was based on items of income and expense that were reported in different years in the financial statements and income tax returns and measured at the rate in effect in the year the differences originated.

(e) Stock Option Plan

The Company has a stock option plan as described in Note 6. When stock options are issued, no compensation expense is recorded. Any consideration received on the exercise of the stock options is credited to share capital.

(f) Hedging

The Company may enter into contracts to manage its exposure to commodity price fluctuations. Gains and losses on commodity price hedges are included in income at the time of the sale of the related production. The Company has not entered into any hedging contracts during fiscal 2001.

(g) Per Share Amounts

Effective January 1, 2001, the Company adopted the new Canadian Institute of Chartered Accountants recommendation for the computation, presentation and disclosure of earnings per share. Basic earnings per common share and cash flow from operations per common share are computed by dividing earnings and cash flow from operations by the weighted average number of common shares outstanding for the period. Diluted per share amounts reflect the potential dilution that could occur if the securities or other contracts to issue common shares were exercised or converted to common shares. The treasury stock method is used to determine the dilutive effect of stock options and other dilutive instruments. The treasury stock method assumes that that proceeds received from the exercise of in-the-money stock options are used to repurchase common shares at the prevailing market rate.

2. BUSINESS ACQUISITIONS

(a) Effective January 2, 2000 the Company purchased all of the shares of Pivotal Energy Corporation ("Pivotal"), a private petroleum & natural gas company, for cash consideration of $218,503 and the issuance of 1,400,000 common shares at a price of $0.50 per common share.

(b) Effective May 1, 2000 the Company purchased all of the shares of Tiara Mining Corporation ("Tiara"), a private petroleum & natural gas company, for cash consideration of $726,913.

The above business acquisitions have been accounted for using the purchase method with the results of operations included in the statement of operations from the effective date of the acquisitions. Details of the business acquisitions are as follows:

	Pivotal	Tiara	Total
Net assets acquired and liabilities assumed:			
Working capital (deficiency)	$ (16,342)	$ 30,000	$ 13,658
Petroleum and natural gas properties	934,845	696,913	1,631,758
	$ 918,503	$ 726,913	$ 1,645,416
Consideration:			
Cash	$ 208,658	$ 700,000	$ 908,658
Common shares issued	700,000	–	700,000
Acquisition costs incurred	9,845	26,913	36,758
Total consideration	$ 918,503	$ 726,913	$ 1,645,416

On June 30, 2000, the Company amalgamated with Pivotal and Tiara continuing as Cigar Oil & Gas Ltd.

3. CAPITAL ASSETS

	2001			2000
	Cost	Accumulated Depreciation	Net Book Value	Net Book Value
Office equipment	$ 60,134	$ 23,131	$ 37,003	$ 40,913
Plant, equipment and gathering systems	1,778,755	129,398	1,649,357	592,445
Petroleum and natural gas properties	8,602,704	1,016,133	7,586,571	2,537,215
	$ 10,441,593	$ 1,168,662	$ 9,272,931	$ 3,170,573

The Company capitalized $226,000 (2000 - $159,800) of general and administrative expenses related to exploration and development activities.

Costs associated with unproven properties excluded from costs subject to depletion total $530,000 (2000 – $205,000). Future development costs of proven undeveloped reserves of $868,000 (2000 - $119,000) are included in the depletion calculation.

A ceiling test calculation as at June 30, 2001 indicated that the estimated future net revenues from proven reserves, at prices and operating costs in effect at the balance sheet date, plus the cost of unevaluated properties less future general and administrative expenses, financing costs, estimated future abandonment costs and income taxes exceeded the net book value of the Company's petroleum and natural gas properties. The ceiling test is a cost recovery test and not intended to result in an estimate of fair market value.

The estimated future site restoration costs to be accrued over the life of the remaining proven reserves were $466,000 (2000 - $320,000). The Company incurred $93,000 (2000 - $1,200) of actual abandonment expenditures during the year.

4. BANK LOAN

The Company has a demand revolving credit facility in the amount of $3,000,000 with a Canadian chartered bank. The facility bears interest at the bank's prime rate plus 1/2 percent and is secured by a $25,000,000 demand debenture and general security agreement conveying a first floating charge with the right to fix all the present and after-acquired property of the Company.

Repayments of the demand revolving credit facility are not required provided that the borrowings do not exceed the lesser of the maximum available and the borrowing base and the Company is in compliance with all covenants, representations and warranties. The facility is subject to a borrowing base review at any time but not less frequently than semi-annually. The current facility expires on September 30, 2001 at which time the Company can request an extension for a period not exceeding one year.

5. INCOME TAXES

The provision for income taxes differs from the result which would be obtained by applying the Canadian basic federal and provincial income tax rate to the net income for the year as follows:

	2001	2000
Net income before income taxes	$ 2,292,636	$ 474,945
Statutory tax rate	42.6%	44.6%
Computed income tax expense at statutory tax rate	$ 976,663	$ 211,825
Non-deductible crown charges	435,884	162,534
Non-deductible depletion	–	55,859
Resource allowance	(447,212)	(103,187)
ARTC	(21,104)	–
Other	3,085	(1,410)
Reduction in future income taxes resulting from reduction in tax rate	(45,642)	–
Utilization of unrecognized non-capital losses	–	(325,621)
	$ 901,674	$ –

The Company has approximately $4,800,000 (2000 - $1,420,000) of tax pools in respect of capital assets available for deduction against future taxable income. In addition, the Company has net-capital losses of $7,630,000 (2000 - $7,630,000) the benefits of which have not been recognized in these financial statements.

A new accounting standard for the recognition, measurement, presentation and disclosure of income taxes has been issued. The new standard requires the use of the liability method of tax allocation accounting whereby the measurement of future tax assets or liabilities will be based on a balance sheet approach rather than the income statement approach under the deferral method. The new standard is effective for the Company's 2001 fiscal year. The Company has adopted the new method effective July 1, 2000 without restating prior years' financial statements. The adoption resulted in an increase in future income tax liability of $1,042,000, an increase in capital assets of $653,000 and decrease in retained earnings of $389,000. The adjustments are a result of recognizing the future tax costs of non-deductible portions of acquisitions and renouncing income tax deductions to flow-through share subscribers. The effect on earnings for 2001 is a reduction in net income of $46,158 with no effect on earning per share.

The components of the net future income tax liability at June 30, 2001 are as follows:

Future income tax assets:	
Future site restoration	$ 1,850
Share issue costs	37,665
	39,515
Future income tax liabilities:	
Capital assets	(1,939,917)
Net future income tax liability	$ (1,900,402)

6. SHARE CAPITAL

(a) Authorized

Unlimited number of common shares
Unlimited number of preferred shares

(a) Issued

	Number	Amount
Balance, June 30, 1999	12,042,693	$ 10,134,165
Private placement to officer	153,846	40,000
Private placement of flow-through share	1,175,100	763,815
Issued on share exchange	1,000,000	276,020
Acquisition of Pivotal Energy Corporation (Note 2)	1,400,000	700,000
Renunciation of flow-through expenditures to investors	-	(652,861)
Share issue costs	-	(3,859)
Reduction in stated capital	-	(8,387,952)
Balance, June 30, 2000	15,771,639	2,869,328
Private placement to officer	340,000	136,000
Private placement	1,500,000	1,125,000
Share issue costs, net of future income tax effect of $43,169	-	(58,166)
Balance, June 30, 2001	17,611,639	$ 4,072,162

The weighted average number of common shares outstanding during the year was 15,972,700 (2000 - 14,360,500)

In June 2001, the Company completed a private placement of 1,500,000 units at $0.75 per unit for gross proceeds of $1,125,000. Each unit consisted of one common share and one-half common share purchase warrant. Each full purchase warrant entitles the holder to acquire one common share of the Company at a purchase price of $1.00 per common share exercisable on or before June 6, 2002. In addition, 100,000 agent's warrants were issued for the purchase of 100,000 common shares at $1.00 per common share exercisable on or before June 6, 2002.

During the year ended June 30, 2000, directors, officers and employees of the Company subscribed for 485,000 of the 1,175,100 flow through shares issued. The Company has incurred and renounced all of its flow-through expenditure commitments.

In July and August 1999, the Company entered into agreements to issue a total of 1,000,000 shares to an officer of the Company. The transactions were completed utilizing a Section 85(1) election of the Income Tax Act. The Company received shares of a publicly traded company and subsequently sold the shares for net proceeds of $276,020. The elected amount of the shares received for income tax purposes was $193,012.

At the annual general meeting of shareholders held November 23, 1999, a special resolution was passed to reduce the deficit of $8,387,952 against stated share capital as of that date.

(c) Stock Options

The Company has adopted a stock option plan under which the board of directors may grant options to directors, officers and key employees for the purchase of common shares at prices determined in accordance with the rules of the Canadian Venture Exchange. Under the plan the Company is authorized to issue options to purchase, in aggregate, up to 10% of the issued and outstanding common shares and the aggregate number of options to any one person cannot exceed 5% of the number of issued and outstanding common shares. The options vest over a two year period and expire not more than five years from the date on which the options were granted. The options outstanding at June 30, 2001 have expiry dates ranging from February 2004 to January 2006. As at June 30, 2001, the Company has reserved 1,577,000 (2000 - 1,310,000) common shares for granting of options.

The change in the number of options outstanding for each of the years ended June 30 are as follows:

	Number		Weighted Average Exercise Price
Outstanding June 30, 1999	770,000	$	0.51
Granted	450,000		0.35
Expired	(120,000)		1.50
Outstanding June 30, 2000	1,100,000		0.34
Granted	250,000		0.40
Expired	(150,000)		(0.36)
Outstanding June 30, 2001	1,200,000	$	0.35
Exercisable, June 30, 2000	583,333	$	0.33
Exercisable, June 30, 2001	933,333	$	0.34

7. PER SHARE AMOUNTS

The Canadian Institute of Chartered Accountants has approved a new standard for the computation, presentation and disclosure of per share amounts. The Company has retroactively adopted the new standard on January 1, 2001. Under the new standard, the treasury stock method is used instead of the imputed earnings method to determine the dilutive effect of stock options and other dilutive instruments. Under the treasury stock method, only "in-the-money" dilutive instruments impact the dilution calculations.

In computing diluted earnings and cash flow from operations per share, 558,000 (2000 - 393,000) shares were added to the weighted average number of common shares outstanding during the year to reflect the dilutive effect of employee stock options. No adjustments were required to reported earnings or cash flow from operations in computing diluted per share amounts.

The 850,0000 common share purchase warrants, as described in note 6 and which were outstanding at June 30, 2001, were excluded from the computation of diluted earnings and cash flow from operations per share since the common share purchase warrants' exercise price was greater than the average market price of the common shares for the period.

The retroactive adoption of the treasury stock method did not result in a change to the reported diluted earnings or cash flow from operations for the year ended June 30, 2000.

8. CHANGES IN NON-CASH WORKING CAPITAL

	2001	2000
Accounts receivable	$ (191,050)	$ (790,218)
Prepaid expenses	(4,320)	(32,069)
Accounts payable	1,814,263	902,582
Acquisition of non-cash working capital	–	13,658
	1,618,893	93,953
Less net change in non-cash working capital related to investing activities	(1,896,367)	(211,544)
Net change in non-cash working capital related to operating activities	$ (277,474)	$ (117,591)
Supplemental disclosure of cash flow information		
Interest paid	$ 37,481	$ –
Income taxes paid	$ –	$ –

9. FINANCIAL INSTRUMENTS

The Company's financial instruments that are included in the balance sheets are comprised of cash, current assets and current liabilities. The carrying values that are included in the balance sheet approximate their fair values due to the short-term maturity of these instruments.

Virtually all of the Company's accounts receivable are with customers and joint venture partners in the petroleum and natural gas industry and are subject to normal industry credit risks.

The Company is exposed to foreign currency fluctuations as petroleum and natural gas prices received are referenced to U.S. dollar denominated prices.

Corporate Information

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BOARD OF DIRECTORS

Robert N. Depoe [3]
Calgary, Alberta

Bernie W. Broda [2]
Calgary, Alberta

Brian H. Gore [1] [3]
Calgary, Alberta

M. H. (Mike) Shaikh [1] [3]
Calgary, Alberta

Richard A. Walls [1] [2] [3]
Calgary, Alberta

(1) Members of the Audit Committee
(2) Members of the Reserve Committee
(3) Members of the Compensation Committee

OFFICERS

Brian H. Gore
Chairman, President & Chief Executive Officer

Bernie W. Broda
Executive Vice President & Chief Operating Officer

David E.T. Pyke
Vice President Land & Contracts

James E. Young
Vice President Exploration

TRANSFER AGENT

Computershare Investor Services Inc.
Calgary, Alberta

SOLICITORS

McCarthy Tétrault
Barristers & Solicitors
Calgary, Alberta

AUDITORS

KPMG llp
Chartered Accountants
Calgary, Alberta

EVALUATION ENGINEERS

Gilbert Laustsen Jung Associates Ltd.
Petroleum Consultants
Calgary, Alberta

BANKERS

CIBC
Calgary, Alberta

STOCK EXCHANGE

Canadian Venture Exchange
Symbol: CGR

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